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May 21, 1993

By Hand Delivery

Donna R. Searcy, Secretary
Federal Communications Commission
1919 M Street, N.W.
Room 222
Washington, D.C. 20554

Re: Comments by the New Jersey Cable Television Association, Inc., Docket RM - 8221

Dear Ms. Searcy:

Attached for filing in Docket No. RM - 8221 are the Comments filed by the New Jersey Cable Television Association, Inc.

If you have any questions, please contact the undersigned.

Respectfully submitted,

John D. Seiver

Attachments

cc: Kathleen Levitz
Gregory Vogt
Peggy Reitzel
ITS

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FEDERAL COMMUNICATIONS COMMISSION
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BEFORE THE
FEDERAL COMMUNICATIONS COMMISSION
Washington, D.C.

In the Matter of	)	
	)	
Amendments of Parts 32, 36, 61,	)	
64, and 69 of the Commission's Rules	)	
to Establish and Implement Regulatory	)	RM - 8221
Procedures for Video Dialtone Service	)	
	)	

COMMENTS

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NEW JERSEY CABLE TELEVISION ASSOCIATION, INC.

May 21, 1993

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FEDERAL COMMUNICATIONS COMMISSION
OFFICE OF THE SECRETARY

BEFORE THE
FEDERAL COMMUNICATIONS COMMISSION
Washington, D.C.

In the Matter of Amendments of Parts 32, 36, 61, 64, and 69 of the Commission's Rules to Establish and Implement Regulatory Procedures for Video Dialtone Service	)	RM - 8221

COMMENTS

The New Jersey Cable Television Association, Inc. ("NJCTA") hereby submits these comments in support of the Joint Petition for Rulemaking and Request for Establishment of a Joint Board ("Joint Petition") filed by the Consumer Federation of America and the National Cable Television Association, Inc. (collectively "CFA/NCTA").[1/]

Introduction and Summary

The Joint Petition seeks commencement of a rulemaking to address the cost allocation and separations issues implicated by the recent spate of video dialtone applications filed by

1/ By Order released April 21, 1993 (DA 93-463) the Commission gave interested parties the opportunity to file comments on the CFA/NCTA Joint Petition by May 21, 1993, with reply comments due June 7, 1993.

certain local exchange carriers ("LECs"). These applications demonstrate the inadequacy of existing rules to control problems with cross-subsidy. Without focusing on these issues in a rulemaking, *ad hoc* determinations will be made on particular applications, with potential inconsistencies and the potential for substantial cross-subsidies due to the individualized nature of the various applications' technical and political configurations.

The Commission should commence a proceeding in which all interested and affected entities may participate to establish these standards rather than making determinations on an application by application basis.2/ Moreover, the tariff review process -- unless modified -- will not protect the ratepayers or competitors from documented and intended cost misallocations. The Commission should establish a formal tariff review plan with express requirements concerning cost calculations and revenue projections in order to insure the proper pricing of the video dialtone services. Finally, a Joint Board is needed to address the complex issue of jurisdictional separations. Use of the public switched

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2/ For example, the various state public service commissions, network for both voice and video requires a separate analysis of the currently existing interstate/intrastate separations formula. All pending video dialtone applications should be held in abeyance until final rules are adopted and the Joint Board established.

I. The Commission Should Grant The CFA/NCTA Petition to Assure Proper Cost Allocation and LEC Compliance With the Video Dialtone Order

NJCTA supports the Joint Petition and also suggests [illegible]

A. Problems With Current Video Dialtone Applications

The announced intention of the Commission's recent Video Dialtone Order was to permit LECs to develop competing video transport facilities for programmers to reach cable television households. Declining to dictate the architecture, the Commission placed confidence in the market to select the most efficient design and facilities. Exhaustively briefed on the potential power of LECs to use their voice ratepayer base to distort the market incentives, the Commission expressly relied upon the processes of the Joint Cost Order[4/] and its authority in the Section 214 certification process to review and apply existing proscriptions against cost misallocation, cross-subsidy, and anti-competitive conduct.

However, certain ambiguities in those existing rules have led to the development and recent deployment of LEC video transport facilities without regard to Commission 214 review or adherence to the principles announced in the Joint Cost and Video Dialtone Orders:

- LECs have deployed the fiber backbone for video dialtone service without submitting their plans to Section 214 review.

4/ Separation of Costs of Regulated Telephone Service From Costs of Nonregulated Activities, Report and Order, 2 FCC Rcd. 1298 (1987)(hereinafter "Joint Cost Order").

° LECs have selectively chosen or restricted their customers to "forum shop" their video services -- sometimes filing tariffs at the FCC to escape more stringent state review of intrastate service offerings while sometimes filing video transport tariffs with the state to ignore FCC limits.

° LECs which have announced their intentions to file federal tariffs are doing so without the cost justification needed to assure the proper allocations and separations under existing FCC orders.

° The GTE Service Corporation ("GTE") petitioned for reconsideration of the VDT Order, asking the Commission to abandon the 214 certification process and rely solely on an abbreviated tariff review process.5/

° GTE's operating companies ("GTOC") filed a new tariff for Videoband-Type II video transport services which is the beginning of a fiber optic network.6/

5/ GTE filed its petition on October 9, 1992. The Florida Cable Television Association ("FCTA"), among others, filed oppositions to GTE's petition.

6/ Tariff Transmittal No. 745, revising GTOC Tariff F.C.C. No. 1. GTOC filed its tariff on October 13, 4 days after GTE petitioned for reconsideration. FCTA filed a petition to suspend that tariff for failure to comply with the Price Caps Order, for discrimination in imposing use restrictions, and for failure to properly structure its rates. After a number of supplemental filings by GTE and FCTA, the Tariff Division denied FCTA's petition to reject the tariff.

° Three pending Video Dialtone applications are disguised channel service applications, but with fiber optic and other substantial costs allocated to basic telephone rate-payers.7/

These developments threaten to undermine the safeguards upon which the Commission has based its Joint Cost and Video Dialtone Orders. NJCTA is vitally concerned not only as a substantial customer of LEC basic telephone and access services, but as a representative of its members providing cable television service to almost two million households in New Jersey. With the current video dialtone applications filed by New Jersey Bell, NJCTA members currently are witnessing explicit attempts to gut the safeguards for competition in the video services transport market that the Commission seeks to promote. "[New Jersey

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7/ Two of the applications, filed by New Jersey Bell Telephone Company, proposed 64 channel systems in Florham Park (W-P-C-6838) and Dover Township (W-P-C-6840), New Jersey. In Florham, New Jersey Bell would cannibalize the existing cable operators' plant and provide 60 channels to subscribers, leaving four available for all competitors. In Dover, New Jersey Bell will construct a completely new distribution and drop facility and again provide 60 channels to FutureVision, leaving four for all other competitors. NJCTA, among others, petitioned to reject the applications on the grounds that New Jersey Bell failed to provide a true video dialtone "gateway" or "platform" by proposing to devote 94% of its capacity to only one customer. Moreover, New Jersey Bell only allocated the "incremental" (not all "direct") ... costs of deploying video capability (ignoring fiber and other electronics' costs) and gave only summary accounting information with inadequate revenue and demand projections to assess whether or not the project satisfied the requirements of Section 214.

Bell's] application is hopelessly inadequate to support Section 214 approval....Its willingness to rush into [...] uncharted waters can rest only on the confidence that its monopoly telephone ratepayers can be counted on for lifeboats."8/ "[New Jersey Bell's] application demonstrates that the threat of cross-subsidy remains alive and well."9/ Moreover, New Jersey Bell's "summary" accounting information effectively prohibited anyone from analyzing the true economics of the proposed video dialtone system. The entirety of New Jersey Bell's presentation obfuscates rather than illuminates the economic (un)reality of the proposal.10/

Both Dr. Johnson and Ms. Kravtin, independent economic consultants, did an analysis of the economic aspects of the New Jersey Bell applications, along with the supporting documentation. Dr. Johnson noted that New Jersey Bell "seeks to justify its application with sweepingly optimistic and unsupported cost and revenue projections,"11/ and characterized the cost data

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8/ Affidavit of Leland L. Johnson, PhD., dated February 12, 1993 ("Johnson Aff.") at 23, submitted as Exhibit E to the Reply of the New Jersey Cable Television Association, filed February 17, 1993 (Docket W-P-C-6840).

9/ Johnson Aff. at 3.

10/ See generally, Affidavit of Patricia Kravtin ("Kravtin Aff."), dated February 16, 1993, submitted as Exhibit F to the NJCTA Reply (W-P-C-6840).

11/ Johnson Aff. at 2.

presented as "utterly worthless".[12] As to New Jersey Bell's projected revenues, Dr. Johnson said "quite literally, if these six digit figures had been generated by a random number machine, we would have no way to detect that fact from [New Jersey Bell's] application."[13] Dr. Johnson offered a critical detailed analysis of the short-comings of the New Jersey Bell application.

Ms. Kravtin as well addressed specific elements of the of the safeguards or determine whether costs are being allocated properly. The Commission clearly needs a different vehicle to make any reasoned analysis of these issues.

The Commission should establish appropriate cost allocation safeguards and confirm that LECs must participate in a thorough tariff review process. All pending video dialtone applications should be held in abeyance until the cost allocation proceedings are completed, rules established specifically for video dialtone evaluations, and a joint board established to resolve the separations issues.[16] These actions are crucial to service offerings to thorough tariff review. A proposed tariff review plan is submitted as Attachment A. This should also be made a subject of the proposed petition for rulemaking.

B. General Problems With LEC Video Services

Before the advent of the video dialtone concept, the Commission was concerned that LEC provisioning of video services could result in an anticompetitive cross-subsidy. These concerns are still valid and point up the need for better rules to deal with new LEC video dialtone applications.

The Commission traditionally reviewed video projects under the 214 certification process. In the 214 process, LECs, like GTE in Cerritos, were ordered to assign all costs for establishing a network to deliver video services "below the line" in order to insulate voice ratepayers from the risk of speculative investments and experiments.[17/] Similarly, in Palo Alto, Pacific Bell also was required to account for its video transport system below the line.[18/]

17/ No costs associated with the construction or operation of the video transport system in Cerritos could appear in any rate base or as an operating expense and all costs were treated as those of an unregulated activity to assure that any short-falls were borne by GTE's stockholders. General Telephone Co. of Calif., 4 F.C.C. Rcd. 5693, 5700 (1989).

18/ Application of Pacific Bell, 68 R.R.2d 1101, 1107 (1991)(no costs associated with the construction, operation, use, The Video Dialtone Order assumed that there would be "ample opportunity" to review LEC video service offerings in the Section 214 certification process, and that existing separations, cost allocation, and accounting protections would apply. VDT Order, ¶¶ 73, 89, 117. The Commission intended to apply the principles of its Joint Cost order to ensure that LEC entry into these services would not harm ratepayers or foment "competition" supported by artificial telco cross-subsidies. Id. at ¶¶ 89-93. Dedicated costs were to be directly assigned and common costs assigned by direct measure of relative use or by general allocation.[19/] Similarly, proper portions of the network must be assigned to the intrastate/interstate jurisdictions to assure that revenues properly matched facility costs.[20/] Without proper separations and allocations, economic costs not recovered from video revenues would be recovered in telephone access charges or in basic telephone service rates -- effectively insulating the LEC and its shareholders from the financial consequences of imprudent investment, while saddling captive telephone customers with those consequences. The Commission was well aware

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19/ Joint Cost Order, 2 FCC Rcd. 1298, 1317-19 (1987). The relative use by general allocator must be based on forward-looking measures to reflect cost-causation principle of these risks, but placed its confidence in its expected review of Video dialtone applications during the Section 214 certification process.[21/]

Historically, most video services have been offered only under interstate tariffs of interexchange carriers like AT&T because the tariffs provided transport for traditional interstate network programming services. By contrast, the interstate access tariffs of LECs do not offer TV transmission services under general rates, nor do most of the LECs' intrastate private line channel tariffs provide for current (non-obsolete) TV channel services. Any video service that the LECs offer today should be treated as a "new service." The Commission expressly forbids Price Cap Carriers from bringing the economics of new services within the unreviewed costs and expenses of other services subject only to price ceilings. Instead, new services introduced by LECs under price caps are to be subjected to more detailed cost support and tariff review scrutiny.[22/] Likewise, the Commission

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21/ The Commission expressly stated its intent to "reassess the adequacy of its existing safeguards" at the time a specific LEC video dialtone proposal is received. VDT Order ¶ 89. Further, the Commission recognized that changes to Part 36 and Part 69 of the rules may be needed to protect against misallocation of costs, and stated that it would deal with such changes in the Section 214 process. Id. ¶ 117. However, as set forth in I(A), supra, Section 214 review of individual applications does not appear suited for establishing general policy guidelines with respect to cost allocation and separations.

22/ The LEC offering new services must submit engineering studies, time and rate studies and other cost accounting

[Footnote Continued Next Page]

already has recognized and confirmed the need to review special access tariffs under existing price cap rules, with additional scrutiny of costs and pricing in view of the special access structure's fundamental redesign to remove barriers to basic service competition.

The Commission must ensure that any future competition for providing video transport services is indeed competitive and subject to the Commission's review and scrutiny at the time any facilities are constructed, or service offered, for video transport. Thus, LECs intending to offer competitive video transport should be expected to submit to such federal tariff review to assure that costs are properly assigned and separated, and that services are properly priced.

Moreover, the LECs must submit to a more realistic separations evaluation. Video dialtone networks will be installed duct space used in common to provide intrastate and interstate services. Even if "interstate", they will be installed using single mode fiber optic facilities that can and would be readily reallocated to be part of the particular LEC's state ratebase, in the event that an LEC's video service offering proved not to be profitable. If "intrastate", because the LEC has artificially limited the customer base to non-media entities, or has pursued another theory to escape FCC jurisdiction, the network nonetheless is the backbone for video dialtone which the FCC expected to pass on in Section 214 review.

Whether jurisdictionally interstate or intrastate, both economics and engineering dictate that these facilities be in common with intrastate facilities. But the manner of separating these facilities is not necessarily rational in the video dialtone situation. Presently, the separations rules do not address the manner in which subscriber lines shall be jurisdictionally separated between the intrastate and interstate jurisdictions in order to take into account the differing network demands imposed by video dialtone service. Current rules indicate that Cable and Wire Facilities costs related to "[s]ubscriber or common lines that are jointly used for local exchange service and exchange access for state and interstate interexchange services" will be separated 75% to the intrastate jurisdiction and 25% to the interstate jurisdiction." 47 C.F.R. § 36.154. The current ratio would allocate to the states three quarters of the loop costs, yet all of the video dialtone revenue would be allocated to the interstate jurisdiction as set out in the New Jersey Bell applications. This would put significant upward pressure on the rates for basic local telephone service. See CFA/NCTA Joint Petition at 12. The LEC should not be able to pick its jurisdiction to evade the interests and review process of the other, while at the same time shifting costs and revenues to suit its needs.

Conclusion

Given the nature and problems with the pending Video Dialtone applications, these issues are ripe and demand the Commission's immediate attention and resolution. It is unreasonable to wait, as the VDT Order assumes, for resolution of these difficult cost and separations issues in the context of patently defective Section 214 applications. It is unreasonable to wait, as the VDT Order elsewhere suggests, for a triennial review of ONA. If a LEC can offer fiber-based video services without detailing its costs and otherwise support its rate structure, the Commission's concerns for maintaining fair competition will be lost. The Commission should commence a proceeding to establish cost allocation standards, refer the separations issues to a Joint Board, and strengthen the tariff review process to include review for compliance with these cross subsidy, cost allocation and separations issues, as proposed in Attachment A, before any video dialtone services may be offered. Otherwise, it may well be too late when a LEC offers a video dialtone service utilizing prepaid or subsidized video facilities.

Respectfully submitted,

NEW JERSEY CABLE TELEVISION ASSOCIATION

By: ______________________
John D. Seiver

EXHIBIT A

IDENTIFYING THE DIRECT ECONOMIC COSTS OF NEW LEC VIDEO TARIFFS

W. P. Montgomery*
Economics and Technology, Inc.

General principles

The Federal Communications Commission's price cap rules for local exchange carriers contain specific requirements for the treatment of newly introduced services. The requirements in these rules with respect to cost support and accompanying workpapers were strengthened in the LEC Price Cap Reconsideration Order.[1] More recently, in recognition that these cost support rules made the initial "net revenue test" for such services somewhat superfluous, the Commission modified application of the net revenue test for local exchange carriers.[2]

Within the scope of these rules it will still be necessary to establish more precise parameters with respect to *specific* new services offered by LECs. This is because the LECs are technically capable of introducing many *different* types of new services, and each type may carry somewhat different cost implications. Some new services may offer new switch-based functionalities, as is the case with tariffs submitted to implement "open network architecture" rules. Other services will offer primarily new transport functionalities.

Some of the new services will primarily provide new offerings within the existing LEC "bottlenecks"; again ONA is an example. The primary concern of the FCC's tariff review process in such instances is to ensure that the new services are not priced excessively, given

[1] 47 CFR §s 61.49(g)(2) and (h).

[2] CC Docket Nos. 89-79 and 87-313, *Memorandum Opinion and Order on Further Reconsideration*, (FCC 92-325), August 6, 1992.

the monopoly nature of the offerings. However, other services that LECs are likely to introduce will address markets where competition already exists. In these circumstances, the tariff review process must be concerned with whether the services are priced too *low*, in an effort by the LEC to enter a market and capture market share too aggressively. Because such services are already being supplied by other firms or are likely to be supplied within the same time frame as the LEC's proposed new service, basic competitive checks usually will prevent the LEC's service from being over-priced.

The tariff review process should have two basic missions with respect to new LEC services that allow the carrier to provide services or facilities in competition with others.

- The first mission is to broadly ensure that the tariff does not impair competition. It is reasonably well-established, however, that the FCC's role is to evaluate the LEC's new service tariff in terms of its potential effect on *competition*. It is not necessarily the FCC's mission to protect *individual competitors*.

Protection of individual firms already operating in the market would not be a policy objective if, for example, data suggest that the incumbent(s) in the market being entered by the LEC are relatively inefficient suppliers, or that the market the incumbent firm(s) serve has somehow been *constrained* by financial, technical or other limits that make the incumbents relatively incapable of satisfying the full potential demand. This concern certainly does not apply to the video transport market. There is no evidence that its current organization leaves any significant component of the video transport market unserved due to the incumbent providers' economic or technological inefficiency. Today, there are many sources for the origination and delivery of video signals, including satellites, CATV systems, ENG microwave links and commercial microwave transport services. Therefore, LEC offerings of new video transport services are unlikely to uniquely satisfy a market requirement that existing providers do not already address.

- The second mission of the tariff review process is to protect the ratepayers of other services and, in doing so, to take account of the important federal-state comity with respect to telecommunications services and facilities that may be allocated either to the interstate or state jurisdiction. In other words, the economic purpose is to foreclose tariffs that could eventually raise costs for customers of *other* services or require state regulators to account for costs that were not covered in the FCC tariff.

This second mission has different ramifications in the video transport market besides ensuring fair competition, although clearly the two tasks are interrelated. The protection of ratepayers carries a *time dimension* that might not be as evident if the sole intent of tariff review were to determine as a threshold matter that the LEC was competing fairly. A particular video services tariff might, for example, be deemed not to be anti-competitive at the time it was introduced, because it might appear to be compensatory at expected levels of demand. But the time dimension in the ratepayer protection objective requires the additional assessment of possible adverse impacts that would occur if the expected demand for the new service failed to materialize.

To put it another way, tariff review under the first point should focus on whether the tariff covers its relevant economic costs in the near term period when the new service would first be offered. Tariff review sufficient to protect ratepayers (and preserve state regulators' ability to do the same thing at their own jurisdictional level) must be able to determine what would happen to the identified costs of the new service *in the event it was not used as heavily as forecasted by the LEC.*

Both of the appropriate economic missions of the tariff review process can be reflected in the data submitted by the LEC with respect to its direct costs and the appropriate amount of the carriers' "just and reasonable overhead costs" under the FCC's existing new services cost submission requirements. The primary question therefore is what types of data and supporting workpapers need to be submitted for this particular class of new services offerings.

IDENTIFYING THE DIRECT ECONOMIC COSTS OF NEW LEC VIDEO TARIFFS

1. ***Start-up costs.*** The LECs cost support should show how it captured the engineering, marketing and business planning costs that went into its decisions to design and offer the service. Such costs should then be amortized over a period representing the initial lifecycle expectation for the services, i.e., the time period in which the first customer or group of customers is expected to utilize the proposed service.

2. ***Costs of existing or newly-installed fiber optics.*** If we assume that fiber optics will be the transport medium of choice (i.e., that any copper plant used in the service offering has no bearing on economic costs), the LEC's cost support should capture the costs of fiber in place that will be utilized in the video transport service. Additionally, because fiber optics lines are far from ubiquitously deployed today, the LEC must show that the unit cost factors that it applies to newly-built entrance facilities or video "loops" are necessary to connect customers or sites to the network. Examples of these cost factors should be displayed in the tariff supporting material even where the LEC proposes to provide new entrance facilities on an individual case basis (ICB). Clearly, if a service offering will depend upon functions that the LEC provides by ICB, then the correct costs of that service cannot be determined unless the cost support for ICBs to be quoted in the future is provided as part of the initial tariff filing.

3. ***Duct, conduit and other space occupied.*** In addition to the basic transport facilities themselves, the new video service cost support should assign a cost for the associated conduit and duct space.[5] This is needed for two reasons. First, it is part of the cost incurred in providing the service. Second, this plant, like the fiber optics lines themselves, likely is highly fungible with other state and interstate services; in the event the video transport service were less than

[5]Many LECs provide pole attachments and conduit space to other firms and it might be possible to impute a carrier's tariff or contract rates for these facilities into the cost support for new video services offerings.